

Commission for Social Development Roundtable: Disappearing Pensions in Rich Countries

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On February 13, 2007, Global Action on Aging hosted a roundtable discussion during the Commission for Social Development focusing on “Disappearing Pensions in Rich Countries.” Ambassador Cho Hyun, Deputy Permanent Representative, Republic of Korea, began by addressing the pension issues facing South Korea. Although South Korea is not yet a rich country, it shares many problems with countries with larger economies. As Korea’s economy has grown, its population growth rate has drastically decreased over the past thirty years from 5 children per family in the 1970’s to currently only 1.1 children per household. South Korea’s status as an emerging economy coupled with its dwindling population growth rate has diverse ramifications, with the most worrying being population ageing.

Their national pension fund, founded in 1988 with limited participation from corporations, expanded until it became a comprehensive, universal pension fund covering all Korean citizens by 1999. The current pension system is a pay as you go system, with the current workforce paying for today’s pensioners. This system is problematic for ageing societies because the debt is always higher than the income. The pay as you go system works well in a society with a growing economy and a growing birthrate, but in country with a dwindling workforce, such as South Korea, the Ambassador believes that the system needs to be reformed. The pension fund is decreasing now and is expected to be completely depleted by 2050. The proposed reforms are to reduce payments to current retirees and increase the contributions of current workers. There also needs to be better management of the pension fund, since previously no attention was paid to investments of pension funds. Before the East Asian financial crisis, many people had invested their entire savings in the stock market because it offered steady growth. As a result, when the financial crisis hit in 1997, many people lost their entire savings and all their pension funds. Thus, investment is needed now in order to cover the ageing population, but savings are also needed in order to avoid repeating the financial crisis. The Ambassador stated that the government should be honest with its citizens and warn them about the looming depletion of the pension fund and encouraging people to buy insurance policies and invest in private pensions as a supplement to the universal fund.

Robin Blackburn

Robin Blackburn, Professor of Sociology at Essex University (UK) and the New School (US), addressed the challenges facing pensioners in the US and the UK, while suggesting solutions for not only the wealthier countries but also as a possible approach for the developing world. Population ageing is not only due to longer life expectancy but also to

lower birth rates. Currently, only 6-7% people in the US and 12-15% in Europe are over 65. By 2035, the number of older persons' in the US will increase to 27%, from 34 million to 70 million.

The question is how much of the national resources are needed and should go to the ageing population. Britain created a Pension Commission responding to the discontent caused by the failure in private funds and the dwindling public funds year after year. The Pension Commission studied the projected costs of how much of the Gross Domestic Produce (GDP) is needed to support retirees. They found that by 2050, just under 14% of the GDP will be needed to provide for the elderly. By 2035, over 13% of the GDP will be needed. The Commission went on to examine if the current pension system could support the projected needs. They found that the public fund will contribute 6% of the GDP while private pensions will have less than 4%, leaving a 4% gap. These essential research findings have determine the size of the challenge and to properly understand the changing demographics and address the needs of the new population. The birth rate in the United Kingdom has already declined, and the life expectancy has already increased.

After identifying the magnitude of the challenge of supporting population aging, the question of how to meet these challenges arises. Some proposed increased immigration to offset the projected expenses needed to cover the elderly, but immigrants provide only 2% of the GDP. After years in the host country, many immigrants adopt the same life patterns as the citizens of the host country, which renders this proposal unsustainable. Moreover, Blackburn pointed out, having wealthy countries depend on the developing world to solve their pension problems seems unethical.

The current "pay-as-you-go" system is highly efficient but it could become burdensome because it raises payroll taxes which eventually suppresses demand and leads to high unemployment rates. In the EU, payroll taxes are being cut in order to try to reverse these effects.

In the US and the UK, a lot of emphasis is placed on private sector provisions and private pensions are heavily subsidized. The private pensions have \$120 billion in the US, but the question begs how much of this fund goes to actual pensioners and how much is absorbed by the costs of the financial industry. Wealthy CEO's, although hard-working and very intelligent, are not ill-rewarded with their pensions. With defined benefits (traditional pensions), a company has a pension fund that distributes pensions for the retirees. The problem, however, is that many companies invest in their own company and since the fund is only backed by the shares in their company if the company declines, then the pensioners do not receive anything. Such was the case with steel, and airline workers.

There has been a shift from defined benefits to defined contributions. Many employers are no longer providing traditional pensions (defined benefits) but are rather giving defined contributions from the society and corporations. This shift has resulted in a cut from 10-15% of employer contributions in the defined benefits system to 3-5% employer contribution in the defined contribution system. This switch also shifts the responsibility

of who is shouldering the risk of the investments of pension funds. Previously, the society and the employer would bear the risk of the investments, whereas now the risk has been shifted to the individual to save as much as he/she wishes and to invest in any way he/she want. If the market crashes, the individual must shoulder the responsibility. Thus, the private sector has a risk factor with the fluctuation of the market.

Tens of millions Americans have personal experience of private pension provision and it has not proved reassuring. Around 1980 just over half the full-time workforce had membership in employer-sponsored pension and healthcare schemes. The formula of tying future benefits to a single employer was unwise in a rapidly shifting industrial environment. The blue chip stocks of one decade became the basket cases of the next. In rising markets companies used to appreciate the rising value of their pension funds and use it as an excuse to skip their own contributions. They now fight shy of the burden of increasingly mature 'defined benefit' (or DB) schemes. When employees' contributions were flooding in everything was fine. But in a classic case of 'bait and switch' some corporations, having under funded their schemes, now seek to dump their liabilities on the public insurer, the Pension Benefit Guaranty Corporation (PBGC). The beneficiaries receive a reduced benefit and the turnaround kings make a killing.

If we scrutinize the projections made by the trustees of Social Security we find that they do include a projection of the tax that will be raised on the pay-out of private pensions. From this figure we can extrapolate the overall size of those pensions. It appears that they will probably never supply more than 2.5 per cent of GDP in the US, hitting that mark in 2018, after which there will be a steep decline to 1.5 per cent of GDP.

Thus, new institutions are needed because both private pension funds and pay as you go systems are insufficient. A reserve fund is needed which can be created by a new kind of tax. Taxing assets and capital, instead of income, would not affect the poor. Also, a corporate tax paid not in cash but in shares would help contribute to a national reserve. Rudolf Meidner, the architect of the Swedish welfare state, first introduced this levy. He urged that corporations should be obliged collectively to contribute to a reserve social fund, which would then be administered by an accountable regional network. While standard corporate taxation subtracts from the cash flow, and thus potentially harms investments and jobs, the Meidner share levy dilutes the value of share-holding but does not weaken operational finances. The levy means that in the future a portion of dividends will go to the social fund network instead of the existing shareholders. If a share levy was set at 10% of profits then it would represent a dilution of share value around 0.7% a year. The fund network would be banned from selling the shares it received and would re-invest earnings for an initial period. By 2035 it would generate income of \$400 billion annually, or 2% of future GDP and could begin to apply them where most needed.

This model could even work in developing countries where there is often a very large discrepancy between the rich and the poor. Also, a global pension could actually be a reality and not just a dream. If a tax of less than .1% of every global transaction was used for a global pension fund, it could save many elderly from abject poverty and lift them

above the dollar a day poverty line. China has taken steps towards a national pension fund by committing all newly privatized company to a 10% corporate tax.

Mark Levinson

Mark Levinson, a senior fellow at the Economic Policy Institute, explained how the US pension system and social security work. He, then, showed the problems of the systems and suggested some remedies.

Contrary to the popular model of the US pension system portraying the system as a three legged stool, Levinson argues that in fact it is more of a pyramid. The three components of pensions (social security, employers' pensions, and workers' savings) are not equal, but are rather built on one another. Social security is the base, the underlying bedrock of the system. Many newspapers and politicians claim that this is the part of the system that is in crisis. Social security, however, is not in crisis. Social Security was never seen as completely adequate to cover the entire system. It was intended as the bedrock, providing the base on which employers' pensions and workers' savings are added.

Employers' pensions, however, is where the crisis actually lies. Defined benefit pensions are being replaced with defined contribution, which are managed by private accounts. With defined contribution pensions, the entire risk is shifted to the individual and that's a problem. Individuals now bear the risk of a market crash, and they are also responsible for how much they put into it. Many workers are not well equipped to manage their own investments. Also, many workers are forced to use these savings accounts to educate their children or for treatment during an illness.

Defined contribution plans are very rapidly replacing defined benefits. Defined contribution plans work very well for the wealthy who can afford to put in large amounts of their monthly income away for their pensions. The top 10% can do better in a defined contribution rather than a defined benefit program, but overall, defined contributions do not help the majority of the population. In fact, they harm the poor who are living from pay check to pay check and cannot afford to put any of their income away. The danger is that not only are companies shifting to defined contribution programs, but so are States. Many States are currently proposing and voting to switch to defined contribution programs.

As for national savings, they are currently non-existent in the US. For the first time since the Great Depression, national savings are negative.

Recently, pensions have come under attack and are constantly being threatened. Only the very wealthy are benefiting from the changes now underway. Thus, the following principles need to be re-established. Every worker should be able to retire at 65 with at least 70 percent of pre-retirement income guaranteed for life. Financing pensions should be equitably allocated among government, employers and workers. Retirement benefits should be portable. Pre-funded retirement assets should be professionally managed to

assure maximum risk adjusted returns and minimize fees. Participants in pre-funded plans should be represented in plan governance.

Barbara Bowen

Barbara Bowen, President of the Professional Staff Congress at CUNY of the American Federation of Teachers, explored how to create the political pressure in order to achieve the proposals suggested by Blackburn and Levinson. The policies of the US makes one wonder who is rich in the rich countries? In other words, who reaps all the benefits in wealthy countries? In New York City, there is an ongoing assault on pension security which was made evident in the NYC transit strike. The strike was not about current benefits but rather about securing pensions for future generations.

A collaboration of the press and political organizations are waging the assault on pension security in New York City. Mayor Bloomberg mentioned in a recent speech that after pension negotiations with unions that the state pension fund is running out. He claimed it will cause the city to go into a \$49 billion deficit. This claim aroused many journalists to call for pension cuts from unions. In response to the claim, a city actuary wrote to the New York Times saying that Mayor Bloomberg's deficit claims were too high and currently all public pension funds are completely funded. In the future, they could potentially be cut from 8%-5.5% but the Mayor's estimates were grossly exaggerated.

During her own union's negotiations with CUNY (City University of New York), Bowen was asked to cut current retiree benefits as part of a compromise that would allow for the University to meet the union's demands. There is a constant assault on pensions pitting retirees against current workers. Bowen and the negotiating team refused to cut retiree benefits and called for a collaboration between older and younger workers.

This assault on pensions is not neutral to race and gender. The first major generation of workers who are persons of color is getting benefits-- but their retiree benefits are constantly being threatened to be pulled out from beneath them. The lowering of pension benefits is a steady and ongoing process whereby every new generation is getting fewer benefits. Therefore, it is important to emphasize that pensions are not a gift, but rather deferred salary. They are earned rights that workers have accumulated over the years. The current assault seems to target public workers more than others because they are the ones benefiting most from public pensions. The resistance to pensions being cut and the shift from defined benefits to defined contributions needs to be organized and stronger. Proposals and ideas on how to solve the problem are essential but they do not stop pensions from being cut. The main reason why there is little public resistance against pension cuts is because pensions have become depoliticized. Defined contributions have made pensions an individual issue and not a social problem. Therefore, in order to stop pensions from being cut, there is an urgent need to re-politicize the issue.

Gender and racial implications of this neo-liberal economic shift are tremendous. Some races are more risk averse than others, which means that defined contribution would effect some groups more than others. The average white person's pension is \$37,000 per

year whereas the average African-American pension is \$24,000 while the average Hispanic pension is 0.